



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

UIL:

507.00-00
4941.00-00
4945.00-00
4947.00-00

Legend:

X =
Y =
Trust =
Trust A =
Trust B =

Dear

We have considered your ruling request dated February 17, 2005, concerning the federal income and excise tax consequences under sections 507, 4941, and 4945 of the Internal Revenue Code ("Code"), relating to a proposed transfer of assets, in the manner and for the purposes described below.

FACTS

X and Y, a married couple, entered into Trust, a charitable remainder unitrust within the meaning of section 664(d)(2) of the Code. Trust is irrevocable.

Trust provides generally that in each taxable year, the trustee shall pay a unitrust amount equal to % of the net fair market value of the assets of Trust valued as of the first day of each taxable year ("Unitrust Amount") to be paid in equal shares to X and Y on the last day of each calendar quarter. If either X or Y dies during the term of Trust, then the Unitrust Amount will be paid entirely to the survivor of X and Y. The payments of the Unitrust Amount will continue until the earlier of (1) the expiration of the twenty year period commencing with the

date X and Y transferred the property to Trust or (2) the death of the second of X and Y to die. Upon the death of the survivor of X and Y, the trustee shall distribute all of the then principal and income of Trust to one or more charitable organizations described in sections 170(c), 2055(a), and 2522(a) of the Code as designated by X and Y, or the survivor of them in a signed writing.

X and Y dissolved their marriage and as part of the marital dissolution, X and Y entered into a Memorandum of Understanding. The Memorandum of Understanding provided that Trust would be divided into two separate and equal trusts, known as Trust A and Trust B. Each trust is intended to qualify as a charitable remainder unitrust under section 664(d)(2) of the Code. As proposed, the assets of Trust will be divided equally in kind between Trust A and Trust B.

Trust A and Trust B will be identical to Trust except that (i) X will be the unitrust beneficiary of Trust A and Y will be the unitrust beneficiary of Trust B; (ii) each spouse will retain a survivorship interest in the other's unitrust amount; (iii) X will have the right to designate the charitable beneficiaries of Trust A and Y will have the right to designate the charitable beneficiaries of Trust B; (iv) X and Y will not be permitted to appoint or change the charitable beneficiaries of the other person's new trust; (v) X will be the sole trustee of Trust A during his lifetime and Y will be the sole trustee of Trust B during her lifetime; and (vi) X and Y will each retain the right to appoint a successor trustee of each person's new trust.

The Superior Court approved a petition by X and Y to divide Trust as stated above. The Court's order, however, is conditioned upon the receipt of a favorable private letter ruling.

RULINGS REQUESTED

You have requested the following rulings:

1. The division of Trust into Trust A and Trust B will not terminate Trust's status as a trust described in, and subject to, the private foundation provisions of Section 4947(a)(2) of the Code and will not result in the imposition of a termination tax under section 507(c).
2. Neither Trust A nor Trust B will be treated as newly created organizations. The aggregate tax benefits of Trust under Section 507(d) of the Code will carry over to Trust A and Trust B in proportion to the amount of Trust assets transferred to Trust A and Trust B, subject to any liability which Trust has under Chapter 42 to the extent not already satisfied by Trust.
3. The division of Trust will not be an act of self-dealing under section 4941(d) of the Code.
4. The division of Trust will not be a taxable expenditure under section 4945 of the Code.
5. If reasonable in amount, payment by the Trust of legal and other expenditures incurred by Trust to effect the proposed division out of the assets of Trust will not constitute an act of self-dealing under section 4941 of the Code or a taxable expenditure under section 4945.

LAW

Under section 4947(a)(2) of the Code, sections 507, 4941 and 4945 apply to certain "split interest" trusts (trusts with both charitable and non-charitable beneficiaries) as if they were private foundations.

Section 507(a) of the Code provides that, except as provided in section 507(b), a private foundation may terminate its private foundation status only under the specific rules set forth in section 507(a).

Section 507(b)(2) of the Code provides that in the case of the transfer of assets of any private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization or reorganization, the transferee foundation shall not be treated as a newly created organization.

Section 507(c) of the Code imposes a termination tax equal to certain defined amounts, which are generally the lower of the "aggregate tax benefit" resulting from the tax exempt status or the fair market value of the assets.

Section 4941(a)(1) of the Code imposes an excise tax on each act of self-dealing between a disqualified person and a private foundation.

Section 4941(a)(2) of the Code imposes an excise tax on the participation of a foundation manager in an act of self-dealing between a disqualified person and a private foundation.

Section 4941(d)(1)(E) of the Code provides that the term "self-dealing" means any direct or indirect transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a private foundation.

Section 4945 of the Code imposes an excise tax on a private foundation's making of any taxable expenditure under section 4945(d).

Section 4945(d)(4) of the Code provides the term "taxable expenditure" includes a grant to a private foundation unless the grantor exercises expenditure responsibility in accordance with § 4945(h).

Section 4946(a)(1) of the Code provides the term "disqualified person" with respect to a private foundation includes a substantial contributor to the foundation (including the creator of a trust), and a foundation manager (including a trustee).

Section 4947(a)(2) of the Code provides generally that split-interest trusts are subject to the provisions of sections 507, 4941 and 4945 in the same manner as if such trusts were private foundations, but, under section 4947(a)(2)(A), not with respect to any amounts payable under the terms of such trust to income beneficiaries, unless a deduction was allowed under section 170(f)(2)(B), 2055(e)(2)(B), or 2522(e)(2)(B).

Section 1.507-3(d) of the Income Tax Regulations ("Regulations") provides that unless a private foundation voluntarily gives notice pursuant to section 507(a)(1) of the Code, a transfer of assets described in section 507(b)(2) will not constitute a termination of the transferor's private foundation status under section 507(a)(1).

Section 1.507-1(b)(6) of the Regulations provides that if a private foundation transfers all or part of its assets to one or more other private foundations pursuant to a transfer described in section 507(b)(2) of the Code, such transferor foundation will not have terminated its foundation status under section 507(a)(1).

Section 1.507-3(c)(1) of the Regulations provides that as used in section 507(b)(2) of the Code, the term "other adjustment, organization or reorganization" shall include any partial liquidation or any other significant disposition of assets to one or more private foundations.

Section 1.507-3(c)(2)(ii) of the Regulations provides that the term "significant disposition of assets" means the transfer of 25% or more of the net assets of the foundation at the beginning of the year, which disposition may be made in a single year or in a series of related dispositions over more than one year.

Sections 1.507-3(a)(1) and 3(a)(2)(i) of the Regulations provide that in the transfer of assets from one private foundation to one or more private foundations in a section 507(b)(2) transfer, each transferee private foundation shall not be treated as a newly created organization, but shall succeed to the transferor's aggregate tax benefit within the meaning of section 507(d) of the Code, in proportion to the assets transferred to each.

Section 1.507-3(a)(9)(i) of the Regulations provides that if a private foundation transfers all of its net assets to one or more private foundations that are effectively controlled, directly or indirectly, by the same person or persons that effectively controlled the transferor foundation, such transferee private foundation shall be treated as if it were the transferor private foundation for purposes of section 4940 through 4948 and sections 507 through 509 of the Code.

Section 1.507-3(b) of the Regulations provides, in pertinent part, that a transfer of assets pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization or reorganization to an organization that is treated as described in section 501(c)(3) of the Code by virtue of section 4947 is not a taxable expenditure under section 4945(d).

Section 1.507-4(b) of the Regulations provides that private foundations which make transfers described in section 507(b)(2) of the Code are not subject to the tax imposed under Section 507(c) with respect to such transfers unless the provisions of Section 507(a) become applicable.

Section 53.4945-6(b)(2) of the Foundation and Similar Excise Taxes Regulations ("Foundation Regulations") provides that expenditures for unreasonable administrative expenses, including compensation, consultant fees, and other fees for services rendered, will ordinarily be taxable expenditures under section 4945(d)(5) of the Code unless the foundation can demonstrate that such expenses were paid or incurred in the good faith belief that they were reasonable and that the payment or incurrence of such expenses in such amounts was consistent with ordinary business care and prudence.

Section 53.4947-1(c)(2)(i) of the Foundation Regulations provides that under section 4947(a)(2)(A) of the Code, section 4941 does not apply to any amounts payable under the terms of a split-interest trust to income beneficiaries unless a deduction was allowed under

section 170(f)(2)(B), 2055(e)(2)(B), or 2522(e)(2)(B) with respect to the income interest of any such beneficiary.

ANALYSIS

Ruling 1

Trust is a charitable remainder unitrust under section 664(d)(2) of the Code , and described in section 4947(a)(2). Therefore Trust is treated as if it were a private foundation and subject to section 507 termination rules. The proposed transfer of 100 percent of Trust's assets, under the prevailing divorce proceedings, to Trust A and Trust B will qualify as transfers meeting the requirements of a "significant disposition of assets" under sections 1.507-3(c)(1) and (2)(ii) of the regulations. Pursuant to section 1.507-1(b)(6), because the transfer of Trust assets to Trust A and Trust B will qualify as a transfer described in section 507(b)(2) the Trust will not terminate its private foundation status under section 507(a)(1).

Under section 1.507-3(d) of the Regulations, the transfer of Trust's assets to Trust A and Trust B will not be considered a voluntary termination of Trust's private foundation status under section 507(a)(1) of the Code because the Trust did not provide notice. According to section 1.507-4(b) since Trust did not voluntarily terminate its private foundation status, Trust will not be subject to tax under section 507(c).

Ruling 2

The proposed transfer division of Trust into Trust A and Trust B, as set forth above, will qualify as transfers meeting the requirements of a "significant disposition of assets" under sections 1.507-3(c)(1) and (2)(ii) of the Regulations. Accordingly, under section 1.507-3(a)(1), the proposed transfer will not result in Trust A and Trust B being treated as newly created private foundations. As provided in section 1.507-3(a)(2)(i), since neither Trust A nor Trust B will be treated as newly created organizations, the aggregate tax benefits of Trust, as described in section 507(a), shall succeed to Trust A and Trust B in proportion to the assets transferred to each.

Ruling 3

Under section 4946(a)(1) of the Code, X and Y are disqualified persons with respect to Trust and are subject to the rules of section 4941. The only interest that either X or Y have in Trust is the payment of the unitrust amount under the provisions of section 664(d)(2). X and Y have exchanged a unitrust (and a contingent survivor's unitrust interest) payment in Trust for a full unitrust payment in Trust A and Trust B, respectively, having fewer assets, namely 50 percent of the assets of Trust, prior to its division. Thus, they are in the aggregate, likely to receive the same unitrust payment as before. Under section 53.4947-1(c)(2) of the Foundation Regulations, the amounts payable under charitable remainder split-interest trusts to income beneficiaries are not subject to section 4941. Thus, the disqualified persons are insulated from self-dealing as far as each of their income interests in Trust are concerned based on the fact that the unitrust payment is the same before and after the division of Trust. Because none of the disqualified persons receive any interest in Trust principal, no self-dealing transaction has occurred within the meaning of section 4941(d).

Ruling 4

Trust is described in section 4947(a)(2) of the Code and is therefore subject to the rules of section 4945. The division of Trust will not be a taxable expenditure under section 4945 of the Code and consequently there will be no obligation on Trust to exercise expenditure responsibility under section 4945(d) and (h). Because Trust A and Trust B are treated as Trust, there are no expenditure responsibility requirements that must be exercised by Trust under sections 4945(d)(4) or (h) with respect to the transfers under section 1.507-3(a)(9) of the Regulations. Therefore, the division of Trust will not be a taxable expenditure and will not result in the exercise of expenditure responsibility.

Ruling 5

Following section 53.4945-6(b)(2) of the Foundation Regulations, legal and other expenses incurred by the Trust in preparation of this ruling request, assuming such expenses are incurred in the good faith belief that they are reasonable and consistent with ordinary care and prudence, will not constitute taxable expenditures. Accordingly, no self-dealing transaction or taxable expenditure will occur within the meaning of sections 4941 and 4945 respectively, to the extent that the expenses are reasonable and proportionate to the Trust's tax risk.

Accordingly, based upon the information submitted in your ruling request, we rule as follows:

1. The division of Trust into Trust A and Trust B will not terminate Trust's status as a trust described in, and subject to, the private foundation provisions of Section 4947(a)(2) and will not result in the imposition of a termination tax under section 507(c).
2. Neither Trust A nor Trust B will be treated as newly created organizations. The aggregate tax benefits of Trust under Section 507(d) will carry over to Trust A and Trust B in proportion to the amount of Trust assets transferred to Trust A and Trust B, subject to any liability which Trust has under Chapter 42 of the Code to the extent not already satisfied by Trust.
3. The division of Trust will not be an act of self-dealing under section 4941(d) of the Code.
4. The division of Trust will not be a taxable expenditure under section 4945 of the Code.
5. With respect to the legal fees and filing fees incurred in the preparation of this ruling request, payment by the Trustee of Trust of a portion of such fees that reasonably represents the portion of this ruling request that is intended to protect the trustee of Trust, will not be an act of self-dealing under section 4941 of the Code and will not be taxable expenditures under section 4945.

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the facts described above under any other provision of the Code. Specifically no opinion is expressed concerning whether Trust qualifies as a charitable remainder trust under

section 644 of the Code or whether Trust A or Trust B each will qualify as a charitable remainder trust under section 664.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept in your permanent records.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

Steven Grodnitzky
Manager, Exempt Organizations
Technical Group 1

Enclosure
Notice 437